

**ANALYSIS OF ORIGINAL BILL**

Author: Runner Analyst: Angela Raygoza Bill Number: SB 612  
 Related Bills: See Legislative History Telephone: 845-7814 Introduced Date: February 27, 2009  
 Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Employer Hiring Credit

**SUMMARY**

This bill would provide a tax credit for a taxpayer who employs qualified employees, as specified.

**PURPOSE OF THE BILL**

It appears the purpose of this bill is to provide a tax incentive to encourage the hiring of individuals receiving unemployment insurance benefits.

**EFFECTIVE/OPERATIVE DATE**

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2009.

**POSITION**

Pending.

**ANALYSIS**FEDERAL/STATE LAW

Current federal law allows employers who hire employees from a "targeted group," as defined, to elect to claim a work opportunity credit (WOTC)<sup>1</sup>. The credit is equal to 40 percent of the qualified first-year wages for that year. The amount of the qualified first-year wages that may be taken into account with respect to any individual shall not exceed \$6,000 per year (\$12,000 per year in the case of any individual who is a qualified veteran).

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

<sup>1</sup> Internal Revenue Code (IRC) 51

Board Position:

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 \_\_\_\_\_ SA      \_\_\_\_\_ O      \_\_\_\_\_ NAR  
 \_\_\_\_\_ N      \_\_\_\_\_ OUA      \_\_\_\_\_ X PENDING

Department Director

Date

Selvi Stanislaus

04/21/09

Under the Government Code, state law provides for several types of geographically targeted economic development areas (G-TEDAs): Enterprise Zones (EZs), Manufacturing Enhancement Areas (MEAs), Targeted Tax Areas (TTAs), and Local Agency Military Base Recovery Areas (LAMBRAs).

Under the Revenue and Taxation Code, existing state law provides special tax incentives for taxpayers conducting business activities within a G-TEDA. These incentives include a hiring credit, sales or use tax credit, business expense deduction, and special net operating loss treatment. Two additional incentives include net interest deduction for businesses that make loans to businesses within G-TEDAs and a credit for employees working in an EZ.

**Hiring Credit:** A business located in a G-TEDA is eligible for a hiring credit equal to a percentage of wages paid to qualified employees. A qualified employee must be hired after the area is designated as a G-TEDA and meet certain other criteria. At least 90 percent of the qualified employee's work must be directly related to a trade or business located in the G-TEDA and at least 50 percent of the employee's services must be performed inside the G-TEDA.

The credit is based on the lesser of the actual hourly wage paid or 150 percent of the current minimum hourly wage (under special circumstances for the Long Beach EZ, the maximum is 202 percent of the minimum wage). The amount of the credit must be reduced by any other federal or state jobs tax credits, and the taxpayer's deduction for ordinary and necessary trade or business expenses must be reduced by the amount of the hiring credit.

Newly enacted state tax law (Calderon, Stats. 2009 Third Extraordinary Session, Ch. 17) allows a credit for taxable years beginning on or after January 1, 2009, for a qualified employer in the amount of \$3,000 for each qualified full-time employee hired in the taxable year, determined on an annual full-time equivalent basis. The credit is allocated by the Franchise Tax Board (FTB) and has a maximum cap of \$400 million for all taxable years. The credit remains in effect until December 1 of the calendar year after the year in which the cumulative credit limit has been reached and is repealed as of that date. Any credits not used in the taxable year may be carried forward up to eight years.

Under current state law, Corporation Tax Law allows the assignment of certain credits to taxpayers that are members of a combined reporting group and adds the following provisions:

- Provides that an "eligible credit" may be assigned by a taxpayer to an "eligible assignee."
  - "Eligible credit" means any credit earned by a taxpayer in a taxable year beginning on or after July 1, 2008, or any credit earned in any taxable year beginning before July 1, 2008, which is eligible to be carried forward to the taxpayer's first taxable year beginning on or after July 1, 2008.
  - "Eligible assignee" means any "affiliated corporation" that is a member of a combined reporting group at certain specified times.
  - "Affiliated corporation" means a corporation that is a member of a combined reporting group.
- Provides that the election to assign any credit is irrevocable once made and is required to be made on the taxpayer's original return for the taxable year in which the assignment is made.

Current state law limits the amount of allowable tax credits for each taxable year beginning on or after January 1, 2008, and before January 1, 2010, to an “applicable amount.” “Applicable amount” is equal to 50 percent of the tax before the application of any credits. Any disallowed credit remains a credit carryover to subsequent years and the credit carryover period is increased by the number of taxable years the credit amount was disallowed. Taxpayers with business income subject to tax of less than \$500,000 are excluded from this law.

### THIS BILL

Beginning on or after January 1, 2009, this bill would allow a tax credit in an amount equal to \$500 per month for each qualified employee employed in a qualified job by the taxpayer. The maximum total amount of the credit that could be allowed for each qualified employee per taxable year would be \$6,000.

This bill would define the following terms:

- “Qualified amount” would be equal to the sum of \$500 per month for each qualified employee employed by the taxpayer in a qualified job, multiplied by the number of consecutive calendar months, not to exceed 12 consecutive months, that the taxpayer employs the qualified employee in a qualified job.
- “Qualified employee” means any person who received unemployment insurance benefits for not less than an unspecified period, prior to the time he or she was hired by the taxpayer for a qualified job.
- “Qualified job” means a non-seasonal, full-time employment position within the State of California that would qualify the employee for benefits under the Unemployment Insurance Code, excluding any benefits received under the Unemployment Insurance Code<sup>2</sup>, and result in a minimum salary of \$1,000 in any month in which the taxpayer seeks to apply the credit.

This bill would allow unused credits to be carried over for six years.

### IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

This bill fails to specify how many months a qualified employee needs to receive unemployment benefits prior to being hired by the taxpayer for a qualified job. By adding a specified period, this would establish what constitutes a “qualified employee” for purposes of this credit. The author should amend the bill to include a timeframe to clarify the requirement and ease administration of this bill.

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<sup>2</sup> Unemployment Code Section 1279.5-defines unemployed and unemployment benefits

This bill is silent regarding the assignment of this business tax credit. Beginning on or after January 1, 2009, a taxpayer that is a member of combined reporting group can assign business tax credits to taxpayers within that group. Assigned credits can only be applied to reduce a tax liability in taxable years beginning on or after January 1, 2010. Consequently, under existing law, any assigned business tax credit would not be claimed until taxable years beginning on or after January 1, 2010. In the absence of language to the contrary, this credit could be assigned to other members of a combined reporting group.

In addition, because this bill provides for a tax credit for the same period for which credits are limited to 50 percent of tax liability, it would be subject to the 50 percent limit under current law. If this is not the author's intent, it is recommended the bill be amended to exclude the credit from the 50 percent limitation.

While this bill specifies that an employer can claim a credit of \$500 per month for each qualified employee, multiplied by the number of consecutive calendar months, not to exceed 12 consecutive months, it is unclear if the bill actually limits the employer to a \$6,000 credit per employee. For example, an employer could claim a tax credit for 11 months, reduce the employee's wages below the \$1,000 threshold for a month or terminate the employee and then rehire the employee the next month and begin the consecutive 12-month period over again for the same employee. If it is the author's intent to provide a limit on the credit, it is recommended that the bill be amended to specify the limit amount.

#### TECHNICAL CONSIDERATIONS

On page 2, line 17 and page 3, line 5, the phrase "seeks to apply the credit" is unclear. Generally, tax credit language uses the phrase "for any month for which the credit is allowed." It is recommended that the language be amended to be consistent with recently enacted tax credit terminology.

#### LEGISLATIVE HISTORY

AB 340 (Knight, 2009/2010) would provide a tax credit for a qualified employer in an amount equal to 5 percent of the wages of all qualified employees employed by the qualified employer during the taxable year. This bill is currently in the Assembly Revenue and Taxation Committee.

ABX3 15 (Stats. 2009, Ch. 10) and SBX3 15 (Stats. 2009, Ch. 17) provide a tax credit of \$3,000 for each net job increase for taxable years beginning on or after January 1, 2009. The credit is allocated by FTB and repealed on December 1 of the following year which the maximum limit of \$400 million is allocated to taxpayers.

SB 508 (Runner, 2009/2010) would provide a tax credit for a qualified taxpayer on the first \$6,000 of wages paid or incurred to a qualified employee. This bill is currently in the Senate Revenue and Taxation Committee.

AB 2365 (Correa, 2003/2004) would have allowed a credit for wages paid to a qualified employee who is hired in the taxpayer's manufacturing trade or business. This bill failed passage out of the Assembly Appropriations Committee.

SB 1523 (Ashburn, 2003/2004) would have allowed a hiring credit to employers with fewer than 19 employees. This bill failed passage out of the Senate Appropriations Committee.

## OTHER STATES' INFORMATION

*Florida* allows businesses located in an EZ a credit based on wages paid to new employees. Other wage-based credits are offered to businesses that are located in high crime or rural areas.

*New York* allows a wage credit to a business that hires a full time employee (either in targeted group or not) for a newly created job in an Empire Zone.

*Illinois* allows a job tax credit for taxpayers conducting a trade or business in an EZ or a High Impact Business. The credit is \$500 for each eligible employee hired to work in the zone during the tax year. The credit is available for eligible employees hired on or after January 1, 1986.

*Massachusetts* allows a Full Employment credit to employers who participate in the Full Employment Program and continue to employ a participant for at least one full month. The taxpayer may claim a credit of \$100 per month of eligible employment per participant, up to \$1,200 per participant.

*Michigan* and *Minnesota* do not offer wage credits.

## FISCAL IMPACT

If the implementation and technical considerations addressed in this analysis are resolved, the department's costs to implement this bill are expected to be minor.

## ECONOMIC IMPACT

### Revenue Estimate

Estimated Revenue Impact of SB 612 As Introduced on February 27, 2009 For Taxable Years Beginning On or After January 1, 2009 Enactment Assumed After June 30, 2009			
Fiscal Year	2009-10	2010-11	2011-12
Revenue Loss	See Discussion Below		

### Revenue Discussion

The revenue impact of this bill would depend on the amount of wages paid to qualified employees by qualified employers and the amount of credits that are used to offset tax liabilities each year. Because the bill fails to specify how long a qualified employee must receive unemployment benefits prior to employment with the qualified employer, an estimate of the revenue impact cannot be determined.

## **POLICY CONCERNS**

Because this bill fails to specify otherwise, a taxpayer could claim the credit proposed by this bill, a deduction for qualified wages, the EZ Hiring Credit or the Local Agency Military Base Recovery Credit , and the newly enacted Job Tax Credit (Calderon, Stats. 2009 Third Extraordinary Session, Ch. 17) using the same employee wages. Generally, a credit is allowed in lieu of any deduction or credit already allowable for the same item of expense in order to eliminate multiple tax benefits.

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of the credit by the Legislature.

## **LEGISLATIVE STAFF CONTACT**

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